IN THE SUPREME COURT, U. S.

United States Supreme Court

Supreme Court, U.S.
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October Term, 1970.

No. 1057

In the Matter of

THE CENTRAL RAILROAD COMPANY OF NEW JERSEY,
Debtor

BONDHOLDERS PROTECTIVE COMMITTEE (of the 3¼% GENERAL MORTGAGE BONDS OF THE CENTRAL RAILROAD COMPANY),
Appellant

C.A. No. 18,549

PETITION OF BONDHOLDERS PROTECTIVE COMMITTEE (of the 3¼% GENERAL MORTGAGE BONDS OF THE CENTRAL RAILROAD COMPANY) FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

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IN THE

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October Term, 1970

No.

In the Matter of

THE CENTRAL RAILROAD COMPANY OF NEW JERSEY,

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BONDHOLDERS PROTECTIVE COMMITTEE (of the 3½% GENERAL MORTGAGE BONDS OF THE CENTRAL RAILROAD COMPANY),

Appellant

C.A. No. 18,549

(Italics supplied unless otherwise noted.)

PETITION OF BONDHOLDERS PROTECTIVE COMMITTEE (of the 3½% GENERAL MORTGAGE BONDS OF THE CENTRAL RAILROAD COMPANY) FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The Bondholders Protective Committee (of the 3½% General Mortgage Bonds of The Central Railroad Company) (hereinafter referred to as the Marx Committee) prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, entered on July 7, 1970.

OPINIONS BELOW

The opinion of the Court of Appeals was filed on July 7, 1970. The opinion has not as yet been reported in the Official Reports and is printed in the Appendix at A5a. The judgment is printed at A1a. A Memorandum Opinion of the District Court for the District of New Jersey is found in the Appendix below at page 2a, and is printed as a convenience to the Court in the attached Appendix at A2a.

JURISDICTION

The judgment of the Court of Appeals for the Third Circuit was entered on July 7, 1970. A Petition for Rehearing was filed on August 13, 1970. Said Petition was denied on September 8, 1970. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1), and 11 U.S.C. 47(c).

QUESTIONS PRESENTED.

1. (a) Does trading in a security of a debtor within 6 months prior to the application by a Bondholders Committee in a Sec. 77 Railroad reorganization proceeding result in the disqualification of such committee?

(b) Does trading by such a committee after its formation result in disqualification?

2. Should Chapter X and Sec. 77 of the Bankruptcy Act be read in pari materia with each other resulting in the disqualification of such committee under Section 77?

3. Where each of the bonds represented by a Bondholders Committee are acquired *after* the Sec. 77 petition is filed by one person (in effect); that person selects each of the members of the committee, none of whom have any financial interest in the debtor; the majority of the said members being present or former employees or associates of said person; should the District Court, (and affirmed by the Court of Appeals) have

disqualified such committee?

4. Is 49 C.F.R. 1117.9(p), requiring a statement by an applicant desiring to solicit authorizations to represent the class merely a *disclosure regulation*, or should a violation result in the disqualification of such applicant?

STATUTES AND REGULATIONS INVOLVED

The following Statutes and regulations are involved herein, the pertinent portions of which are printed in the Appendix at A00 to A00:

Bankruptcy Act, Sec. 77(c)(13), 11 U.S.C. Sec. 205(c)(13):

> (13) The judge may on his own motion or at the request of the Commission refer any matters for consideration and report, either generally or upon specified issues, to one of several special masters who shall have been previously designated to act as special masters in any proceedings under this section by order of any court of appeals and may allow such master a reasonable compensation for his services and actual and reasonable expenses. The court of appeals of each circuit shall designate three or more members of the bar as such special masters whom they deem qualified for such services, and shall from time to time revise such designations by changing the persons designated or their number, as the public interest may require: *Provided, however*, That there shall always be three of such special masters qualified for appointment in each circuit who shall hear any matter referred to them under this section by a judge of any district court. The debtor, any creditor or stockholder, or the duly authorized committee, attorney or agent of either or the trustee or trustees of any mortgage, deed of trust or indenture pursuant to which securities of the debtor are outstanding, shall have the right to be heard on all questions arising in the proceedings, and upon petition therefor and cause shown, any such person or any other interested party may be permitted to intervene. The judge may, after hearing, make reasonable rules defining the matters upon

which notice shall be given to other than interveners and the manner of giving such notice.

Bankruptcy Act, Sec. 77(p); 11 U.S.C. Sec. 205(p)

(p) It shall be unlawful for any person, during the pendency of proceedings under this section or of receivership proceedings against a railroad corporation in any State or Federal court, (a) to solicit, or permit the use of his name to solicit, from any creditor or shareholder of any railroad corporation by or against whom such proceedings have been instituted, any proxy or authorization to represent any such creditor or shareholder in such proceedings or in any matters relating to such proceedings, or to vote on his behalf for or against, or to consent to or reject, any plan of reorganization proposed in connection with such proceedings, or (b) to use, employ, or act under or pursuant to any such proxy or authorization from any such creditor or shareholder which has been solicited or obtained prior to the institution of such proceedings, or (c) to solicit the deposit by any such creditor, or shareholder, of his claim against or interest in such railroad corporation, or any instrument evidencing the same, under any agreement authorizing anyone other than such depositor to represent such depositor in such proceedings or in any matters relating to such proceedings, including any matters relating to the deposited security or claim, or to vote such claim or interest or to consent to or reject any such plan of reorganization; or (d) to use, employ, or act under or pursuant to any such agreement with such depositor which has been solicited or obtained prior to the institution of such proceedings; unless and until, upon proper application by any person proposing to make such solicitation or to use, employ, or act under or pursuant to such proxies, authorizations, or deposit agreements, and after consideration of the terms and conditions (including provisions governing the compensation and expenses to be received by the applicant, its agents and attorneys, for

such solicitation or to use, employ, or act under or pursuant to such proxies, authorizations, or deposit agreements, the Commission after hearing by order authorizes such solicitation, use, employment, or action: *Provided, however*, That nothing contained in this section shall be applicable to or construed to prohibit any person, when not part of an organized effort, from acting in his own interest, and not for the interest of any other, through a representative or otherwise, or from authorizing a representative to act for him in any of the foregoing matters, or to prohibit groups of not more than twenty-five bona fide holders of securities or claims or groups of mutual institutions from acting together for their own interests and not for others through representatives or otherwise or from authorizing representatives of such groups to act for them in respect to any of the foregoing matters. The Commission shall make such order only if it finds that the terms and conditions upon which such solicitation, use, employment or action is proposed are reasonable, fair, and in the public interest, and conform to such rules and regulations as the Commission may provide. The Commission shall have the power to make such rules and regulations respecting such solicitation, use, employment, or action and with respect to the terms and the provisions of such proxies, authorizations, and deposit agreements, and with respect to such other matters in connection with the administration of this subsection as it deems necessary or desirable to promote the public interest, and to insure proper practices in the representation of creditors and stockholders through the use of such proxies, authorizations, or deposit agreements and in the solicitation thereof. It shall be unlawful for any person to solicit any such proxy, authorization, or the deposit of any such claim or interest or to use, employ, or act under or pursuant to any such proxy, authorization, or deposit agreement which

has been solicited or authorized prior to the institution of such proceedings in violation of the rules and regulations so prescribed.

Every application for authority shall be made in such form and contain such matters as the Commission may prescribe. Every such application shall be made under oath, signed by, or on behalf of, the applicant by a duly authorized agent having knowledge of the matters therein set forth. The Commission may modify any order authorizing such solicitation, use, employment, or action by a supplemental order, but no such modification shall invalidate action previously taken, or rights or obligations which have previously arisen, in conformity with the Commission's prior order or orders authorizing such solicitation, use, employment, or action.

The Commission may, in its discretion, make such investigations as it deems necessary to determine whether any person has violated or is about to violate any provision of this subsection (p) or any rule or regulation thereunder, and may require or permit any person to file with it a statement in writing, under oath, or otherwise as the Commission shall determine, as to all the facts and circumstances concerning the matter to be investigated. The Commission is authorized, in it discretion, to publish information concerning any such violations, and to investigate any such facts, conditions, practices, or matters as it may deem necessary or proper to aid in the enforcement of the provisions of this subsection (p), in the prescribing of rules and regulations thereunder, or in securing information to serve as a basis for recommending further legislation concerning the matters to which this subsection relates.

Bankruptcy Act, Ch. X, SS 209-212; 11 U.S.C. SS 609-612

Sec. 209. Any creditor or stockholder may in a proceeding under this chapter act in person, by an attorney at law, or by duly authorized agent or committee.

Sec. 210. An attorney for creditors or stockholders shall not be heard unless he has first filed with the court a statement setting forth the names and addresses of such creditors or stockholders, the nature and amounts of their claims or stock, and the time of acquisition thereof, except as to claims or stock alleged to have been acquired more than one year prior to the filing of the petition.

Sec. 211. Every person or committee, representing more than twelve creditors or stockholders, and every indenture trustee, who appears in the proceeding shall file with the court a statement, under oath, which shall include

(1) a copy of the instrument, if any, whereby such person, committee, or indenture trustee is empowered to act on behalf of creditors or stockholders;

(2) a recital of the pertinent facts and circumstances in connection with the employment of such person or indenture trustee, and, in the case of a committee, the name or names of the person or persons at whose instance, directly or indirectly, such employment was arranged or the committee was organized or formed or agreed to act;

(3) with reference to the time of the employment of such person, or the organization or formation of such committee, or the appearance in the proceeding of any indenture trustee, a showing of the amounts of claims or stock owned by such person, the members of such committee or such indenture trustee, the times when acquired, the amounts paid therefor, and any sales or other disposition thereof; and

(4) a showing of the claims or stock represented by such person or committee and the respective amounts thereof, with an averment that each holder of such claims or stock acquired them at least one year before the filing of the petition or with a showing of the times of acquisition thereof.

Sec. 212. The judge may examine and disregard

or warrant of attorney, trust mortgage, trust indenture, or deed of trust, or committee or other authorization, by the terms of which an agent, attorney, indenture trustee, or committee purports to represent any creditor or stockholder, may enforce an accounting thereunder, may restrain the exercise of any power which he finds to be unfair or not consistent with public policy and may limit any claim or stock acquired by such person or committee in contemplation or in the course of the proceeding under this chapter to the actual consideration paid therefor.

49 C.F.R. 111-7.9(p) (Rule 58.9(p))

§ 1117.9 Contents of application.

Each applicant shall show, in the following order:

* * * * *

(p) Whether the applicant, any of his affiliated interests, or any of his immediate family, have within 6 months prior to the date of the application, purchased or sold any securities or other obligations of the debtor or of any of its affiliated interests.

STATEMENT OF FACTS.

The facts may be summarized as follows.

1. On October 23, 1967, the Bondholders Protective Committee (hereinafter referred to as the Marx Committee) applied to the United States District Court for the District of New Jersey for leave to intervene in the proceedings for the reorganization of The Central Railroad Company of New Jersey, filed under Section 77 (11 U.S.C. Sec. 205) of the Bankruptcy Act. The District Court reserved decision on the motion, pending the disposition of an application to the Interstate Commerce Commission for authority to solicit authorizations to represent all the bondholders of the debtor railroad under Section 77(p), 11 U.S.C. 205c (13).

2. The original application of the Marx Committee to the I.C.C. was made on July 13, 1967. The I.C.C. withheld action on the application pending a hearing. At the first hearing, held

on *October 18, 1967*, Messrs. Murray M. Salzberg and Morris H. Snerson appeared and answered that they "intended" to form another Bondholders Committee for the *same class*. (249a)

3. On or about *November 10, 1967*, Messrs. Murray M. Salzberg and Morris H. Snerson organized a Committee which they called "3¼% Mortgage Bondholders Protective Committee" (hereinafter referred to as the Salzberg Committee).

4. Thereafter, said Salzberg Committee filed a like application for leave to solicit authorizations pursuant to the Statute.

5. After several hearings, the Hearing Examiner filed his report on May 24, 1968, in which he recommended that the application of the Marx Committee be denied, and the application of the Salzberg Committee granted.[1] On September 13, 1968, Division 3 of the I.C.C. entered an Order in conformity with said recommendation, except for certain modifications. Thereafter, the Marx Committee applied for reconsideration, and on December 11, 1968, the application was denied.

6. On or about January 24, 1969, the Marx Committee filed a complaint in the United States District Court to set aside or enjoin the enforcement of the Order. While said complaint was still pending, both Committees were granted leave to move their applications for leave to intervene.[2]

7. On October 1, 1969, the District Judge denied the application of the Marx Committee for intervention, and granted the application of the Salzberg Committee. On appeal to the Court of Appeals for the Third Circuit the said Order was confirmed.

8. The transcripts of the several hearings before the Hearing Examiner were admitted into evidence before the District Court on the applications for intervention. The proofs,

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[1] Another application was filed by Fred G. Wolff, et als, with the I.C.C. That application was denied by the Hearing Examiner. (55a; 67a)

[2] The complaint was subsequently dismissed by the District Court, on appeal the Court of Appeals affirmed (No. 18,356). A companion petition for certiorari has been filed in this Court.

as disclosed by the record before the District Court and the Court of Appeals, disclose the following:

A. The Marx Committee was composed of five business and professional men, all residents of the State of New Jersey, and all of whom were the legal or beneficial owners of the bonds in issue *long prior to the institution of the reorganization proceedings*. In addition, in a supplement to the Marx Committee application, the Committee stated that one Paul Benton, C.P.A., had agreed to act as a consultant to the Committee if the application for intervention was granted. His qualifications are set forth in the record. (32a-35a, 160a-163a)

B. The I.C.C., in effect, determined that the Marx Committee was fully qualified to act for the class. However, the I.C.C. then determined that the Salzberg Committee was *better* qualified than the Marx Committee, by reason of the fact that the latter Committee were ostensibly the owners of some $3.8 million face amount of debtor's bonds (out of a total of some $42 million) and the alleged railroad experience of its members. (88a-89a) The I.C.C., as well as the District Court and the Court of Appeals, refused to pierce the facade of said "Committee". The actual facts, as disclosed by the record, are set forth below.

1. The original Petition for Reorganization under Section 77 was filed by Central on March 22, 1967 (14a). The Marx Committee was formed on May 5, 1967 (13a), and the application to the I.C.C. was filed on July 13, 1967. However, the hearing on said application was deferred by the I.C.C. to October 18, 1967.

2. At said hearing, Messrs. Salzberg and Snerson appeared before the Hearing Examiner at which time the Examiner took the testimony of the applicants as well as that of Morris H. Snerson. Mr. Snerson stated at that time that he and his associate, Murray M. Salzberg, then owned *jointly* 3¼% bonds of Central to the extent of *$3,509,000.00* and that they intended to form a second bondholders committee. *On November 14, 1967*, Messrs. Salzberg, et als, filed an application with the I.C.C. for leave to solicit authorizations on behalf of their Committee, which was formed *on November 10, 1967* (40a).

At the hearing held on October 18, 1967, the witness

berg, then owned (jointly) Central bonds to the extent of $3,509,000.00 (84-85b). He further testified that they intended to form a bondholders committee (86), that they started to purchase the bonds in *"May of 1967"* (86), that they are aware of the fact that the original Petition by Central was filed on *March 22, 1967* (88), that he was aware of the fact that the market price of the bonds had gone down since March 22, 1967 (89), that between March 22, 1967, and October 18, 1967, neither he nor his associate took any steps to form a bondholders' committee (90).

At the hearing held on January 24, 1968, the witness Snerson testified as follows:

(a) That he and his associate (Murray M. Salzberg) owned bonds (as of said date), having a face value of $4,613,000.00 (103-104), that said bonds were acquired "sometime in May, starting with May of 1967, *and were acquired up to the time when we placed our application to the Interstate Commerce Commission*" (105), that each of the members of the Committee (ultimately formed by them) were selected and designated by them (105).[4]

(b) A notice to produce the original bonds was ignored (126-127). It was admitted, however, that

[3] All page references hereinafter relate to the transcripts of the hearings before the I.C.C. marked as Exhibit 2 through 4. They are also reproduced in the Appendix below, commencing at 164a.

[4] From the foregoing it is evident that Messrs. Snerson and Salzberg acquired additional bonds in the face amount of $1,004,000.00 between October 18, 1967, when they first announced their intention to form a second committee, and November 14, 1967, when the application was filed with the I.C.C. It is also clear that additional bonds were purchased between November 10, 1967, *the date of the formation of the committee*, and November 14, 1967, *when the application was filed*.

the bonds were acquired in part from borrowed money (130).

(c) *That none of the other members of the Committee personally owned any bonds or had any financial interest in Central (131-132)*

(d) That the bonds were purchased by Messrs. Salzberg and Snerson for "investment" – despite the fact that on March 22, 1967, when Central filed its Petition under Section 77, it showed an accrued deficit for 1965 in the sum of $44,908,227.00, for the year 1966 in the sum of $51,944,057.00 (1966 Annual Report – Exhibit 7-313a).

(e) That the only members of the Committee who resided in the New York Metropolitan area were Messrs. Murray M. Salzberg, Morris H. Snerson, and Roger Snerson (son of Morris H. Snerson).

(f) That the other members of the Committee resided (respectively) in LaGrange Park, Illinois; Boone, Iowa; Morrisville, Vermont; and Fayetteville, New York (a suburb of Syracuse).

(g) That, out of the seven members of the Committee, Messrs. Roger Snerson, Louis A. Putnam, and Michael C. Jacobs, were then present or former employees or associates of Messrs. Salzberg and Morris H. Snerson (153-171); that none of the members of the Committee (allegedly selected by Messrs. Salzberg and Snerson for their expertise), had made a study of the operations of Central as of the date of the hearing held on November 14, 1967.

REASONS FOR GRANTING THE WRIT.

1. THE COURT OF APPEALS HAS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW WHICH HAS NOT BEEN, BUT SHOULD BE SETTLED BY THE SUPREME COURT (RULE 19-1b).

The basic question before the Court of Appeals was whether the Salzberg Committee was disqualified from acting as a fiduciary for the class in view of the following admitted facts in the record:

owned (jointly) by Messrs. Salzberg and Snerson.

(b) That each of said bonds was acquired, in part, from undisclosed borrowed funds, *after the institution of the reorganization proceeding*.

(c) That following the announcement before the Hearing Examiner that Messrs. Salzberg and Snerson intended to form a bondholders' committee, they acquired additional bonds in the face amount of $1,004,000.00[5]; that *after the formation of the committee, on November 10, 1967, they acquired additional bonds (105; 268a)*

(d) That the majority of the members of the Committee were present or former employees or associates of Messrs. Salzberg and Snerson, and were hand-picked by them.[6]

(e) That the majority of the members of said Committee resided at places far removed from the location of the "res".[7]

In its argument before the District Court, the Marx Committee asserted that the comparable provisions of Chapter X of the Bankruptcy Act, and particularly 11 U.S.C. Section 609-13; and 11 U.S.C. Section 649 should be read in *pari materia* with Section 77p (11 U.S.C. Section 205p). The

[5] It is basic that "trading" involves either purchase *or* sale of the security of the debtor. It has also been held that the comparable provision under Chapter X (Section 249; 11 U.S.C. Section 649) must be "strictly" construed. See Collier on Bankruptcy, 14th Ed. Vol. 5, P. 1013, et seq.

[6] It is true that Section 77(p) provides that a person in interest may act through "a representative or otherwise". However, it is submitted that the Statute never contemplated the situation where one person in interest (acting jointly in the case at bar) may act for themselves, *and in addition*, select five other persons. This would only lead to the type of abuses which have been repeatedly condemned by the S.E.C. and the Courts. See Collier 14th Ed. Vol. 6A, P. 346, et seq.

[7] The record of the proceedings shows that Central's operations are basically confined to the States of New Jersey and Eastern Pennsylvania, and that its principal headquarters are located in the City of Newark, New Jersey.

District Court found "no merit in this argument". In its opinion, the Court of Appeals stated, in pertinent part, as follows:

> "The Marx Committee charged the principal members of the Salzberg Committee with engaging 'in open and flagrant trading in the debtor's bonds after they had announced their intention to form a committee' and therefore claimed that the interests of bondholders cannot be fairly and adequately protected by the Salzberg Committee.[1]
>
> "(1)" The Marx Committee cites no authority which prohibits such alleged transactions. The claim that the provisions of Chapter 10 of the Bankruptcy Act, particularly 11 U.S.C.A. §§609-13, should apply to this Chapter 8 proceeding can hardly be sustained in the face of 11 U.S.C.A. §501 'The provisions of this chapter (i.e. Chapter 10) shall apply *exclusively* to proceedings under this chapter.' (Emphasis added)."

We submit that both the District Court and the Court of Appeals clearly committed error. In view of the rising tide of railroad reorganizations, this question should be resolved without delay by the Supreme Court, *since there are no present decisions at any level on this important issue.*

It is clear that despite the provisions of 11 U.S.C.A. Section 501, supra, Section 77 is an integral part of the whole Bankruptcy Act, and should be read in *pari materia* with Chapter X. See Collier on Bankruptcy, 14th Ed. Vol. 5, page 4001 from which we quote:

> "77.01. Legislation Development of §77.
>
> "Section 77 was added to the Bankruptcy Act as part of Chapter 8 by the Act of March 3, 1933, and was amended slightly by the Act of June 7, 1934. In 1935, however, the provision was completely rewritten. The general plan of §77 as enacted in 1933 was retained, but it was rearranged, somewhat simplified and clarified, and generally made more practical and workable." (Footnotes omitted).

It is evident from the foregoing that Section 77 was added as part of Chapter 8 of the Bankruptcy Act. Under the

circumstances, all of the provisions of the Bankruptcy Act should be read *part materia*, including Chapter X. Cf. *Hallenbeck v. Penn Mutual Life Insurance Company*, 323 Fed. 2nd 566, 571 (4th Cir. 1963), from which we quote:

> "Although the provisions of Chapter XI are expressly declared to apply exclusively to proceedings thereunder, we are of the opinion that decisions pertinent to proceedings under Chapter XI (applicable only to *unsecured* creditors) may be helpful in the construction of Chapter XIII provisions respecting the jurisdiction and injunctive power of the bankruptcy court.
>
> "(3) It is well settled that statutes which relate to the same persons or things, or the same class of persons or things, or have a common purpose may be regarded as 'part materia.' Furthermore, similar statutory provisions in *part materia* should receive similar and harmonious construction. 50 Am. Jur., Statutes, §§ 348-351 (1944). In view of the similar language, the simultaneous enactment of these debtors' statutes by the same legislative body and the similar purposes to be served thereby, we hold that the statutes comprising Chapters X, XI, XII and XIII of the Bankruptcy Act are *in part materia* and that the construction so uniformly given to sections 311 and 314 of Chapter XI should be equally applicable to sections 611 and 614 of Chapter XIII of the Act. Additionally, the legislative history of Chapters XI and XIII reveals that section 311 of the Chapter XIII were derived from the same source, and that section 314 of Chapter XI and section 614 of Chapter XIII were derived from the same source." (Footnotes omitted.)

See also in re *Missouri Pacific R R Co.*, 24 Fed. Supp. 724, 729 (D.C.E.D. Mo. 1938) affirmed 104 F. 2nd 1 (8th Cir. 1939), cert. denied 308 U.S. 559 (1939).

Sub-section (p) of Section 77 was adopted in 1935 (Act of August 27, 1935, 49 Stat. 911). It was designed to curb abuses found to exist in railroad reorganization proceedings. The Hearing Examiner recognized this legislative policy in his

report, from which we quote: (76a, et seq.)

"Subsection (p) of section 77 of the Bankruptcy Act was enacted in 1935, and with other revisions of the act then made was designed to curb abuses found to exist in court and Commission proceedings in connection with railroad reorganizations. Section 77, enacted early in 1933, had extended the coverage of the Bankruptcy Act to railroad reorganizations, and had vested in the Commission, acting in conjunction with the Federal court, jurisdiction over plans of reorganization of railroads in the formative stages. As originally enacted, however, section 77 contained no provision for regulation of protective committees or of solicitation of proxies to represent railroad stockholders or holders of railroad securities in reorganization proceedings. In practice, control of such committees had largely passed into the hands of speculative interests or of those interests which were responsible for the insolvent railroad's difficulties and sought to perpetuate their hold thereover without regard to the legitimate interests of the railroad's stockholders and creditors. For a single stockholder or bondholder to protect his interests in a reorganization proceeding is impractical in most instances, as the cost of counsel fees alone would make such participation prohibitive. However, by a pooling of their resources behind an aggressive committee with active and competent counsel, the investor or creditor is able to make his voice heard in the reorganization proceedings and to protect his investment. In the absence of effective regulation, and by the use of proxies and deposit agreements under which the investor virtually surrendered control of his stock certificate or bond, manipulators were able to wrest control of these protective committees. Subsection (p) was enacted to put an end to such sharp practices and to protect the public from exploitation."

Pursuant to its authority, the I.C.C. adopted a regulation which provides that with respect to an application to solicit

authorizations under Section 77, the applicant must show, among other things, "whether the applicant, any of his affiliated interests, or any of his immediate family, have, within six months prior to the date of the application *purchased or sold any security or other obligations of the debtor or any of its affiliated interests*". (49 C.F.R. 1117.9(p)).

It will be noted that the foregoing regulation does not set forth any penalties for a violation. It is clear, however, that the said regulation is strikingly similar to Sections 210 and 211 of Chapter X (See Collier on Bankruptcy 14th Ed. Vol. 6A, 331 et seq.).As stated by the authors of Collier, commencing at page 351:

> "Chapter X enables the reorganization judge to exact of representative agencies or bodies a standard of personnel and conduct which attains the fullest measure of protection to the principal, secures a conscientious representation of his interests, and which is responsive to his rights and needs along.
>
> "Trading in securities by a committee, agent or other representative is especially condemned by Chapter X. Such activity violates the character of the service and the singleness of the interest which a security holder's representative should maintain in his behalf. The fiduciary nature of the relationship makes conduct of this sort particularly undesirable, regardless of the general integrity of the representative, the lack of profit in the transaction, or the fact that purchases were made in the open market or of claims or interests not within the scope of the purchaser's representative authority."

Under Chapter X of the Bankruptcy Act the trading in securities of the debtor by a committee or other representative of the security holders is considered to be a breach of fiduciary duty, and the Court has the power to disqualify a committee if they violate their duty as a fiduciary. See, e.g., *Matter of Realty Asso. Securities Corp.*, 56 F. Supp. 1008 (E.D. N.Y. 1944), wherein the Court granted an application to disqualify a Bondholders Committee, stating:

"A bondholder (creditors) committee is a fiduciary

for all bondholders and as such owes undivided loyalty and allegiance to the bondholders, and to them alone.

"No one has questioned seriously the control of the reorganization Court over protective committees in Chapter X reorganications. The legislative history (Sen. Rep. No. 1916, 75th Congress 3d Sess. (1938) 33), the statutory provisions (Bankruptcy Act, Sections 209-212 inclusive, 11 U.S.C.A., SS 609-612), and the statements of the United States Supreme Court (*Securities and Exchange Commission v. United States Realty & Improvement Co* (U.S.Sup. Ct.) 310, U.S. 434, 448-450, 42 Am. B.R. (N.S.) 602, 60 S. Ct. 1044, 84 L. Ed. 1293) document the Court's authority to scrutinize the authorizations of committees to act, and to take such reasonable measures as it may be advised will protect the interested parties."

In view of all of the foregoing, it is clearly evident that the Court of Appeals, as well as the District Court, should have adopted the principles relating to the status, duties and obligations of a Committee seeking to represent other persons of the same class, as outlined by the authors of Collier, from which we quote:

"From this it is evident, as indeed the Supreme Court has held, that a committee . . . representing claimants or security holders in a reorganization proceeding occupies a fiduciary position. While 'it is clear that an honest, intelligent and energetic committee may often be in a position to render valuable, if not indispensable, services to the security holders it represents', it is equally clear that from the nature of the services to be performed, 'the fullest measure of aid and protection to the investor demands a conscientious representation of his interests by persons who are responsive to his needs, appreciative of his rights, and single in their loyalty to his interests.' The Supreme Court has warned that 'the most rigorous responsibilities for fair dealing upon those who respresent the rights of others. . . . Conse-

quently those who purport to act for members of the investing public should serve only one master, and if they fail to abide by this single standard they are subject to whatever judicial action may be necessary such as disqualification . . . to correct their dereliction." (*Collier on Bankruptcy*, 14th Ed., Vol. 6A, page 337, et seq.) (Footnotes omitted.)

See also Collier on Bankruptcy 14th Ed. Vol. 6A, page 1013, et seq.

It has been repeatedly stated that Courts of Bankruptcy are essentially Courts of Equity. See *Guaranty Trust Co. of New York v. Henwood*, 86 F. 2d 347 (8th Cir. 1937), cert. denied 300 U.S. 661, 57 S. Ct. 492 (1938); *In re New York, O. & W. Ry. Co.*, 25 F. Supp. 709 (D.C., N.Y. 1938). Accordingly, such a Court is committed to scrutinize the proceedings in order to bring about a just and equitable result and should not be bound by rigid legal postulates.

In view of all of the foregoing, it would be anomalous, indeed, if the acts and conduct of Messrs. Salzberg and Snerson, as outlined hereinabove, should receive a Judicial stamp of approval, whereas similar acts and conduct by a Committee under Chapter X would result in the sanctions outlined in the Statute and cases. It is true, as the Court of Appeals indicated, that we were unable to cite any authority for our objection to the Salzberg Committee. The apparent reason for the paucity of cases under Section 77 is that no group of creditors or stockholders in the recent past has had the effrontary and audacity to follow the methods used by the Salzberg Committee outlined above in the face of the sordid history of Railroad reorganization referred to in the Hearing Examiner's report, supra. See also Sen. Rep. No. 1916, 75th Congress 3d Sess. (1938) 33.

CONCLUSION

For all of the foregoing reasons, we respectfully submit that this Petition should be granted.

Respectfully submitted,

ALLAN L. TUMARKIN
Attorney for Petitioner

DATED: November 12, 1970.

JUDGMENT OF COURT OF APPEALS
Filed: Sept. 16, 1970

UNITED STATES COURT OF APPEALS
For the Third Circuit

No. 18,549

IN THE MATTER OF THE CENTRAL RAILROAD COMPANY OF NEW JERSEY, *Debtor*

BONDHOLDERS PROTECTIVE COMMITTEE (of the 3¼% GENERAL MORTGAGE BONDS OF THE CENTRAL RAILROAD COMPANY), *Appellant*

(D. C. Bankruptcy No. B-401067)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Present: BIGGS, STALEY and ADAMS, *Circuit Judges*

JUDGMENT

This cause came on to be heard on the record from the United States District Court for the District of New Jersey and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the order of the said District Court, filed October 1, 1969, be, and the same is hereby affirmed, with costs taxed in favor of appellee.

ATTEST:

Clerk

July 7, 1970

OPINION OF DISTRICT COURT
Filed October 1, 1969

Applications for leave to intervene in these proceedings have been filed by the Bondholders' Protective Committee, hereinafter the "Marx Committee", and the 3¼% Mortgage Bondholders' Protective Committee, hereinafter the "Salzberg Committee". The bonds involved are the Debtor's General Mortgage Bonds, 3¼% Series, due July 1, 1987, with respect to which the Manufacturers Hanover Trust Company is the Indenture Trustee.

At the time of the filing of their respective applications, the Marx Committee alleged an authorized representation of bondholders owning $405,000.00, face amount, later reduced to $345,000.00 of Debtor's bonds, and the Salzberg Committee alleged an authorized representation of bondholders owning $4,613,000.00, face amount, of such bonds. The hearing on these applications was adjourned from time to time to await the outcome of proceedings brought by both Committees before the Interstate Commerce Commission to determine which Committee should be permitted to solicit authorizations from the holders of Debtor's bonds to represent and act for them pursuant to Section 77(p) of the Bankruptcy Act, 11 U.S.C.A. § 205(p).

Intervention, generally speaking, in pending civil litigation is governed by Rule 24 of the Federal Rules of Civil Procedure. More specifically, in a railroad reorganization, Section 77(c)(13) of the Bankruptcy Act, 11 U.S.C.A. § 205(c)(13), provides that:

> "[t]he debtor, any creditor or stockholder, or the duly authorized committee, attorney or agent of either of the trustee or trustees of any mortgage, deed of trust or indenture pursuant to which securities of the debtor are outstanding, shall have the right to be heard on all questions arising in the proceedings, and upon petition therefor and cause shown, any such person or any other interested party may be permitted to intervene."

With respect to these rival applications for intervention, the Court has had the benefit of the arguments of counsel,

briefs submitted in behalf of their clients, and the record of the Section 77(p) hearing before the Interstate Commerce Commission. That hearing, of course, and the objective sought thereby, is entirely different from the pending applications for intervention. Despite this difference, the expertise of the Interstate Commerce Commission should not be overlooked in its evaluation of the Marx and Salzberg Committees in connection with their applications for approval to solicit authorizations from the Debtor's bondholders. The Court would be remiss if it did not seek enlightenment from the observations and findings made by the Commission on the composition of the two Committees and the qualifications of their members.

Counsel for the Marx Committee, in support of his argument that the Salzberg Committee should not be allowed to intervene, ascribes great weight and authority to allegedly analogous situations in Chapter X proceedings under the Bankruptcy Act. It is argued that the provisions of Chapter X, dealing with disqualification of committees formed to represent security holders, should be read pari materia with Section 77(p) of the Bankruptcy Act. there is no merit to this argument. While it is true that certain provisions of the Bankruptcy Act have been made applicable to Section 77 proceedings, it is evident that there is no need to go beyond the provisions of that Section to determine the criteria for intervention.

The principal objective of a Section 77 proceeding is the speedy and economical reorganization of a railroad. Every effort should be made to simplify procedures to attain that end. Intervention necessarily carries with it the addition of another and independent party to the litigation, represented by its own attorney, and in many cases, also by counsel. In exercising its discretion in matters of intervention, the Court must be mindful of the duplication of time, effort and expense that would be occasioned by the unnecessary addition of parties to the litigation. To allow every possible interested party or group to intervene in this case would seriously curtail the orderly conduct of the proceedings and greatly increase the expenses of administration, and this Debtor, as must be evident to all parties, can ill afford added financial burdens. Accordingly, the Court concludes that intervention by only

one of the two rival Committees is necessary to adequately protect the interests of the public and the bondholders.

The Court is satisfied, and finds, upon a consideration of the record in this case, that the Salzberg Committee will afford the better protection for the interests of the Debor's bondholders in the reorganization proceedings. The substantial holdings of that Committee, and the capabilities and qualifications of its members, as reflected in the report of the Interstate Commerce Commission, should serve as an appropriate complement to the representation of the bondholders now being exercised by the Manufacturers Hanover Trust Company, Indenture Trustee under the mortgages securing Debtor's bonds. This determination, however, does not disqualify the members of the Marx Committee from participating in their own behalf, as bondholders, at different stages of the proceedings.

Where a class is already adequately represented, the Court may properly refuse intervention to other members of that class. Therefore, in light of this Court's Findings and conclusions as herein set forth, the petition of the Marx Committee for leave to intervene generally in these proceedings will be denied, and that of the Salzberg Committee to intervene generally in the proceedings will be granted, and it is so

ORDERED, this 1st day of October, 1969.

ANTHONY T. AUGELLI
United States District Judge

OPINION OF COURT OF APPEALS
Filed: July 7, 1970

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 18,549

IN THE MATTER OF THE CENTRAL RAILROAD COMPANY OF NEW JERSEY, *Debtor*

BONDHOLDERS PROTECTIVE COMMITTEE (of the 3½% GENERAL MORTGAGE BONDS OF THE CENTRAL RAILROAD COMPANY), *Appellant*

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

Argued June 18, 1970

Before BIGGS, STALEY and ADAMS, *Circuit Judges*

OPINION OF THE COURT

(Filed July 7, 1970)

PER CURIAM:

We are asked here to review another denial by the District Court of an application by an interested party to intervene generally in the Central Railroad Company of New Jersey ("debtor") reorganization. The issue presented is whether Chief Judge Augelli abused his discretion in

denying the petition to intervene filed by the Bondholders Protective Committee.

The reorganization proceeding was instituted on March 22, 1967, in the United States District Court for the District of New Jersey, pursuant to Section 77 of the Bankruptcy Act, 11 U.S.C.A. §205. The Bondholders Protective Committee ("Marx Committee"), representing $345,000 face amount of debtor's bonds, and the 3¼% Mortgage Bondholders' Protective Committee ("Salzburg Committee"), representing more than $3.5 million face amount of debtor's bonds, each applied to the District Court pursuant to 11 U.S.C.A. §205(c)(13) for leave to intervene in the debtor's reorganization proceeding.

The arguments for intervention were heard by the District Court after proceedings brought by each committee before the Interstate Commerce Commission ("ICC") to determine which committee should be permitted to solicit authorizations from the debtor's bondholders pursuant to 11 U.S.C.A. §205(p). The transcript of hearings before, and report of, the ICC were introduced into evidence by the Marx Committee at the hearing and oral argument before Chief Judge Augelli of these applications to intervene. The District Court denied the application of the Marx Committee to intervene, and granted that of the Salzburg Committee. The Notice of Appeal filed by the Marx Committee stated that it was appealing "from the Order denying the application of said Committee to intervene in the above cause." Although we have serious doubts concerning what matters are properly raised by such notice of appeal (see Rule 3(c), Federal Rules of Appellate Procedure), we have considered both portions of the District Court's order—the one granting the motion to intervene by the Salzburg Committee and the one denying the motion to intervene by the Marx Committee.

The Marx Committee concedes that under Rule 24, Federal Rules of Civil Procedure, and 11 U.S.C.A. §205(c)(13), general intervention in Section 77 proceedings may properly be denied where a class is already adequately

represented. See generally 5 Collier on Bankruptcy PP 77.08 (14th Ed. 1969). The Marx Committee charged the principal members of the Salzburg Committee with engaging "in open and flagrant trading in the debtor's bonds after they had announced their intention to form a committee", and therefore claimed that the interests of bondholders cannot be fairly and adequately protected by the Salzburg Committee.[1] Chief Judge Augelli, however, found that the Salzburg Committee would represent fairly and adequately the interests of all the bondholders, and that intervention by others would merely complicate and make more expensive the reorganization.

Upon review of the record before the District Court, we are of the opinion that Judge Augelli did not abuse his discretion in granting the motion of the Salzburg Committee to intervene and denying that of the Marx Committee. *Cf.* In re Central Railroad Co. of New Jersey, 391 F.2d 417 (1968). As Judge Augelli noted, nothing prohibits the members of the Marx Committee from appearing on behalf of themselves from time to time as provided in 11 U.S.C.A. §205(p).

Accordingly, the order of the District Court will be affirmed.

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1. The Marx Committee cites no authority which prohibits such alleged transactions. The claim that the provisions of Chapter 10 of the Bankruptcy Act, particularly 11 U.S.C.A. §§609 13, should apply to this Chapter 8 proceeding can hardly be sustained in the face of 11 U.S.C.A. §501: "The provisions of this chapter [i.e. Chapter 10] shall apply *exclusively* to proceedings under this chapter." (Emphasis added.)

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit